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SIPDIS

SENSITIVE

STATE FOR NEA/ELA, NEA/RA, AND EB/IDF
USAID FOR ANE/MEA MCCLLOUD
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COMMERCE FOR 4520/ITA/ANESA/TALAAAT

E.O. 12958: N/A

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SUBJECT: PRIVATIZING SUGAR MAY BE BITTER IN THE SHORT TERM

Sensitive but Unclassified. Please protect accordingly.

Summary

1. (SBU) The Egyptian Ministry of Investment (MOI) recently announced plans to sell 36% of Delta Sugar, a joint venture company, in an initial public offering (IPO). Announcement of the sale follows an earlier announcement that another public sector sugar producer, El Nobareyah, would be put up for sale. MOI's privatization plans for the sugar industry have drawn criticism from parliamentarians, who blame the proposed sales for the recent increase in consumer sugar prices. MOI claims the consumer price increase is the result of domestic demand outstripping domestic production and rising import prices. The food ration system also appears to have been affected by the increase in sugar prices, as ration-card holders report reduced sugar rations or none at all. In addition, the GOE has increased its projected budget for food subsidies by 80% for the coming fiscal year. MOI's long-term plan to meet Egypt's sugar demand is solicitation of private sector investment in the sugar industry to expand domestic production. MOI may be using sugar as a test case for privatization of public sector food production companies. End summary.

Is privatization the problem...

2. (U) The MOI recently announced plans for partial privatization of Delta Sugar Company, Egypt's largest producer of beet sugar, through an IPO. Delta is a joint venture company, of which the GOE owns 87.9%. Thirty six percent of the GOE's shares in the company will be sold in the IPO over the next two months. Press reports indicate that MOI is still considering sale of the remaining public shares, possibly to an anchor investor. Prior to announcement of the Delta IPO, MOI also placed another public sugar company, El-Nobareyah Sugar, up for sale. El Nobareyah, established in November 2004, is still in its development phase and has not yet begun producing sugar. MOI has also indicated that the largest public sugar company - Sugar and Integrated Industries Co. (SIIC) - though not yet slated for sale, may also be privatized.

3. (U) MOI's privatization plans for the sugar industry have stirred controversy in the People's Assembly (PA), where the concept of privatization finds little support. Shortly after announcement of the Delta IPO, the Industrial Committee of the PA voiced is strong opposition to the move. Parliamentarians blamed MOI's privatization plans for the recent increase in sugar prices in the Egyptian market. Since early February, consumer prices for sugar have risen from approximately LE 2.50-2.75/kg to as high as LE 3.60/kg in some stores.

...or Egypt's sweet tooth?

4. (U) According to MOI, the rise in sugar prices has less to do with privatization than with the imbalance in Egypt's sugar consumption vis--vis its production. Although Egypt is the largest producer of sugar in the Middle East, it is also the largest sugar consumer, with domestic demand considerably outstripping production. In 2005, Egypt produced 1.36 metric tons (MT) of sugar but consumed 2.5 MT. Imports covered the nearly 50% gap, with Brazil taking first place as Egypt's largest foreign source (0.98 MT in 2005, of a total 1.2 MT in sugar imports). The recent rise in world sugar prices is therefore the main cause of the increase in consumer prices in Egypt, according to MOI. The price of imported sugar rose from LE 1625 (\$285)/ton to LE 2519 (\$440)/ton between January and March 2006.

Short (term) and not sweet

15. (U) The discrepancy between Egypt's production and consumption of sugar also has implications for the GOE's food ration system, a Nasser-era program that provides free monthly rations of basic food items to certain pensioners, widows, orphans and various other disadvantaged populations. Despite statements in the press from the Ministry of Trade and Industry that Egypt has sugar reserves of 660 thousand tons, equivalent to 7 months of imports, ration-card holders have reported receiving less than their full sugar quota or no sugar at all. On March 4, the GOE announced that 4 items in the ration basket, pasta, margarine, beans and lentils, would be eliminated over the next two months and the ration of sugar increased from 1 to 2 kilos per month. The redistribution of goods in the ration basket allows the GOE to accommodate the rise in sugar import prices without increasing the budget for that particular program. The budget projection for the overall food subsidy program, however, has risen dramatically. The GOE recently announced that it would increase its budget allocation from LE 35.3 billion to LE 56 billion - an 80% increase - in FY 2006/07 to cover increases in prices of imported consumer goods, including sugar.

16. (U) The MOI has indicated in press reports that it plans to increase Egypt's sugar production in the long term by issuing tenders for new private-sector investment projects in the sugar industry. Aiming for investments of approximately LE 1.1 billion, the tenders would increase beet sugar recovery by adding a new line that would increase production at the Daqahliyya Sugar Company - another public sector firm - by 25,000 tons. Additional tenders will be issued to construct a new factory to produce 250,000 tons of sugar. MOI also believes that partial privatization of other sugar companies may improve the operating methods and efficiency of the companies.

Comment

17. (SBU) MOI's plans for partial privatization of the sugar industry are the first to touch on the food production sector. That the plan is for partial rather than full privatization indicates that the GOE is either not comfortable divesting the entire public stake in this sector or is testing public reaction before proceeding with additional privatization in the food industry. Currently MOI has plans to sell minority shares in 4 flour mills by the end of FY 2005/06 (i.e., by June 30, 2006). Flour is likely to be even less price-elastic than sugar as bread is a staple for Egypt's poor. End comment.